THE BRAVE NEW WORLD OF ARBITRATION

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Once, long ago, arbitration was a method of dispute resolution that the courts viewed with skepticism. Those days now are only a distant memory. In 1925, Congress laid the groundwork for change when it passed the Federal Arbitration Act.[1] At first, outside the realms of organized industrial relations and international commercial transactions, little seemed different. It was not even clear to what extent the new federal policy on arbitration applied only to the federal courts, and to what extent it affected state courts and state law as well. In 1964, in *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*,[2] the Supreme Court signaled that a new and favorable day had dawned for arbitration. Perhaps this was because the pressure of exploding dockets was beginning to make itself felt; perhaps legal philosophers who had long urged the use of more harmonious methods of dispute resolution were making headway; perhaps, as class actions were becoming popular in the wake of the 1966 amendment to Federal Rule of Civil Procedure 23 and as discovery was becoming an expensive burden, people were looking for ways to simplify litigation.

Whatever the reason, there can be no denying that from *Prima Paint* through the 2001 decision in *Circuit City Stores, Inc. v. Adams*,[3] the Court has systematically dismantled the remaining legal constraints that stood in the way of the recognition of agreements to arbitrate, the enforcement of such agreements, and the enforcement of the resulting arbitral awards. It has federalized the law of arbitration to a degree astonishing to those who have thought of the Rehnquist Court as the new expositor of states' rights and federalism. It has expanded the availability of arbitration far beyond the law merchant and collective bargaining to all parts of the non-criminal legal world, so that it now encompasses, in addition to those traditional subjects, practically all statutory claims, constitutional claims, consumer claims, and employee claims. The Court has turned away efforts to place limits on what it takes to form a pre-dispute contract for arbitration and has found voluntary

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1 The Act was originally called the United States Arbitration Act; *see* Act of Feb. 12, 1925, Ch. 213, §§ 1 et seq. In 1954, it was renamed the Federal Arbitration Act, and is now codified in Title 9 of the United States Code.

2 388 U.S. 395 (1967).

3 532 U.S. 105 (2001).

consent to arbitration even if the contract was presented on a take-it-or-leave-it basis, even if actual notice of the arbitration clause is doubtful, and even if there were marked disparities in bargaining power between the parties.

It would be too much to say that a backlash has developed to the apparent triumph of arbitration. But doubts are springing up that a one-size-fits-all arbitral regime is optimal. Recent court decisions refusing to enforce some kinds of arbitration agreements and some arbitral awards display a new caution and concern for public policies that may be suffering as arbitration sweeps across the legal landscape. In today's talk, I would like briefly to review the key Supreme Court decisions that have brought us to where we are today, and then turn to the new issues that those decisions have brought to the fore and the skeptical undercurrents that can be detected in the courts. I conclude that arbitration in the United States today is still a work-in-progress. Some recalibration of the system is necessary and desirable if we are to reach a socially acceptable balance between dispute resolution in the public institutions known as courts and private dispute resolution that should be entitled to public enforcement.

I. SUPREME COURT LANDMARKS

While the topic of arbitration arose from time to time in Supreme Court decisions after the passage of the Arbitration Act in 1925, for the most part the cases involved either industrial relations (especially in the railroad industry, where the Railway Labor Act has long required a special form of mediation and arbitration) or highly specialized areas, such as disputes between states or admiralty cases. One interesting exception to that pattern, however, arose in *Hardware Dealers' Mut. Fire Ins. Co. v. Glidden Co.*,[4] a case involving the constitutionality of a Minnesota statute that required arbitration of the question of amount of loss in all fire insurance policies written in that state. The Supreme Court upheld the state law over a challenge based on the due process and equal protection clauses of the Fourteenth Amendment. It acknowledged that the arbitration process might not have been strictly voluntary, because it was imposed by statute. Nevertheless, it went on to say that "the procedure by which rights may be enforced and wrongs remedied is peculiarly a subject of state regulation and control."[5] The state rationally might have singled out amount of loss as a topic well suited to arbitration procedures because of the frequency of disputes on that point, the need for speedy determinations, and the special utility of expert knowledge. The opinion concluded as follows:

"Granted, as we now hold, that the state, in the present circumstances, has power to prescribe a summary method of ascertaining the amount of loss, the

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4 284 U.S. 151 (1931).

5 *Id.* at 158.

requirements of the Fourteenth Amendment, so far as now invoked, are satisfied if the substitute remedy is substantial and efficient."[6]

The Court also added that the state was free to choose any kind of remedy "provided its choice is not unreasonable or arbitrary, and the procedure it adopts satisfies the constitutional requirements of reasonable notice and opportunity to be heard."[7] The *Hardware Dealers* case thus stands as an early example of a hospitable reception of arbitration as a method of dispute resolution, albeit one with some important qualifications that may not have lost their relevance.

The next important case, *Wilko v. Swan*,[8] was decided in 1953. It posed the question whether an arbitration agreement between a securities brokerage firm and one of its customers was enforceable. The Supreme Court said "no", on the ground that the agreement to arbitrate amounted to a waiver of rights conferred by the Securities Act of 1933 and thus was void under section 14 of that Act. The Court recognized that the United States Arbitration Act "establish[ed] by statute the desirability of arbitration as an alternative to the complications of litigation,"[9] but it thought that the mere existence of the arbitration statute did not resolve the question of the way it related to section 14 of the Securities Act. It rejected the respondent's argument that "arbitration [was] merely a form of trial to be used in lieu of a trial at law,"[10] for several reasons. First, it thought that section 14 reflected the view of Congress that buyers and sellers of securities would typically occupy unequal bargaining positions and have asymmetrical access to information. Second, waiver of a judicial forum deprives the buyer of more options than it does the seller. Third, there is no assurance in arbitration that the arbitrators would be properly instructed in the law or that they would apply the law correctly. The latter point was especially troublesome because section 10 of the Arbitration Act, as the Court noted, provides for such a narrow range of review that mistakes would go uncorrected. Finally, and most broadly, the Court intimated (while reserving the point) that the right to select a forum might be a substantive right in itself and that an agreement restricting that choice might thwart the express purpose of the statute.

The next major arbitration case in the Supreme Court, *Prima Paint*,[11] arose out of a more conventional arbitral dispute: whether one party had performed as required under a simple consulting services contract. The

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6 *Id.* at 159.

7 *Id.* at 158.

8 346 U.S. 427 (1953); later overruled by the Supreme Court in Rodriguez de Quijas v. Shearson/American Express, Inc., 490 U.S. 477 (1989).

9 346 U.S. at 431.

10 *Id.* at 433.

11 Prima Paint Corp. v. Flood & Conklin, Mfg., 388 U.S. 395 (1967).

contract contained a broad arbitration clause that required arbitration under the rules of the American Arbitration Association over "[a]ny controversy or claim arising out of or relating to this Agreement, or the breach thereof. . . ."[12] The wrinkle was that one party, Prima Paint, argued that the other party, Flood & Conklin, had committed fraud in the inducement of the agreement that contained the arbitration clause. Prima Paint took the position that a charge of fraud in the inducement had to be resolved by the court before any arbitration of the underlying claim could go forward. The Supreme Court disagreed. It held that section 4 of the Federal Arbitration Act (FAA) required a court to order arbitration to proceed once it was satisfied that the making of the agreement to arbitrate was not at issue. In so holding, it distinguished sharply between a challenge to the formation of the contract "generally" (which is all that Prima Paint was asserting) and challenges to the formation of the agreement to arbitrate within the contract: "We hold, therefore, that in passing upon a § 3 application for a stay while the parties arbitrate, a federal court may consider only issues relating to the making and performance of the agreement to arbitrate."[13]

This rule, the Court went on to state, was a rule of federal law, enacted under the "incontestable federal foundations of 'control over interstate commerce and over admiralty.'"[14] It therefore made no difference that the case before it was a diversity case. The federal court was bound to apply the FAA, and in the absence of any challenge to the making of the contract generally, it was required to stay the litigation so that the arbitration could proceed. Any other questions about fraud in the inducement generally could be presented to the arbitrator.

While the tone of *Prima Paint* was indisputably more favorable toward arbitration than had been the case in *Wilko*, that difference might have been explained by the respective subject matters at hand: statutory claims, in *Wilko*, versus private law, in *Prima Paint.* Perhaps that explanation was accurate at the time. But in the next key case, the Court took a cautious step toward opening the door to the arbitration of statutory claims.

That case was *Scherk v. Alberto-Culver Co.*,[15] which seemed like a reprise of *Wilko v. Swan* with two potentially important differences: first, the claim arose under section 10(b) of the Securities Exchange Act of 1934, and SEC Rule 10b-5, and second, the transaction was an international one. Petitioner Scherk was a German citizen residing in Switzerland; he transferred ownership of three enterprises he owned to Alberto-Culver, along with certain warranties relating to trademarks. The sales contract contained an arbitration

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12 *Id*. at 398.

13 *Id.* at 404.

14 *Id.* at 405.

15 417 U.S. 506 (1974).

clause committing the parties to arbitrate any claims that arose out of their agreement or its breach, using the facilities of the International Chamber of Commerce in Paris, and applying Illinois law. When problems arose about a year later, Alberto-Culver sued in federal district court in Illinois for damages and other relief, relying specifically on section 10(b) of the Exchange Act and Rule 10b-5. Scherk moved to dismiss for want of personal and subject matter jurisdiction, and on the basis of *forum non conveniens,* but most importantly for present purposes, he also moved to stay the action pending ICC arbitration. Alberto-Culver resisted on the basis of *Wilko* – an argument accepted by both the district court and the court of appeals.

The Supreme Court reversed and found that the arbitration clause was enforceable. It offered a half-hearted distinction between section 14 of the 1933 Act and the comparable section of the 1934 Act, but it then assumed for the sake of argument that the two were functionally identical. It was the international aspect of the case that persuaded the Court to uphold the arbitration arrangement. It noted the difficult choice of law questions that could arise when the parties are from different countries; the conflicts over the actual choice of forum; and the need to be able to structure international business in an orderly fashion. As it had done for choice of judicial forum clauses in *The Bremen v. Zapata Off-Shore Co.,*[16] it eschewed "a parochial refusal . . . to enforce an international arbitration agreement."[17] Quoting from *The Bremen,* the Court held that

> [a]n agreement to arbitrate before a specified tribunal is, in effect, a specialized kind of forum-selection clause that posits not only the situs of suit but also the procedure to be used in resolving the dispute. The invalidation of such an agreement in the case before us would not only allow the respondent to repudiate its solemn promise but would, as well, reflect a "parochial concept that all disputes must be resolved under our laws and in our courts . . . ."[18]

This was one of the first times that the Court so frankly equated dispute resolution in courts with dispute resolution in arbitral tribunals (though a hint of that appears even in *Hardware Dealers*),[19] but it was not to be the last.

The Supreme Court's decision in *Southland Corp. v. Keating*[20] expanded the availability of arbitration in a different way: at a stroke, the Court federalized the law of arbitration and provided the basis for finding federal

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16 407 U.S. 1 (1972).

17 *Scherk,* 417 U.S. at 516.

18 *Id.* at 519 (quoting *The Bremen,* 407 U.S. at 9).

19 *See supra* note 4 and accompanying text.

20 465 U.S. 1 (1984).

preemption of any state law that purported to treat arbitration less favorably than the FAA. Briefly, California had a franchise protection statute which, as authoritatively construed by the California Supreme Court, made pre-dispute agreements to arbitrate disputes between franchisees and franchisors unenforceable. The U.S. Supreme Court found that this law "directly conflict[ed] with § 2 of the Federal Arbitration Act and violate[d] the Supremacy Clause."[21] It reasoned that the FAA as a whole rested "on the authority of Congress to enact substantive rules under the Commerce Clause."[22] Substantive rules of this kind, it went on, must be applied in state courts as well as federal courts. Congress would not have accomplished its goal in 1925 of reversing the ancient hostility to arbitration agreements if it had not ensured that the FAA norms had to be applied to state legislation as well. It is interesting to note that Justice O'Connor, joined by then-Justice Rehnquist, dissented from this holding. She concluded that section 2 of the FAA (which specifically says "[i]f any suit or proceeding be brought in any of the courts of the United States") was addressed only to the federal courts. Her dissent closed with the following trenchant observation:

> Today's decision is unfaithful to congressional intent, unnecessary, and, in light of the FAA's antecedents and the intervening contraction of federal power [referring to the overruling of *Swift v. Tyson* in *Erie*], inexplicable. Although arbitration is a worthy alternative to litigation, today's exercise in judicial revisionism goes too far.[23]

After *Southland*, the pace of Supreme Court decisions encouraging the use of arbitration quickened. Three cases eliminated any doubt about the arbitrability of public law, statutory claims: *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,[24] *Shearson/American Express, Inc. v. McMahon*,[25] and *Rodriguez de Quijas v. Shearson/American Express, Inc.*[26] *Mitsubishi* held that antitrust claims arising in an international context were arbitrable, extending the rule of *Scherk*. *McMahon* held that domestic Exchange Act cases arising under Rule 10b-5 were arbitrable, and then *Rodriguez de Quijas* definitively overruled *Wilko*. Other equally important statutory claims received the same treatment. In *Gilmer v. Interstate/Johnson Lane Corp.*,[27] the Supreme Court held that a claim under the Age Discrimination in

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21 *Id*. at 10.

22 *Id.* at 11.

23 *Id.* at 36.

24 473 U.S. 614 (1985).

25 482 U.S. 220 (1987).

26 490 U.S. 477 (1989).

27 500 U.S. 20 (1991).

Employment Act (ADEA) could be subjected to compulsory arbitration pursuant to an arbitration agreement in a securities registration application. The *Gilmer* Court was not persuaded that the public policies embodied in the ADEA would be undermined if these claims were resolved through arbitration, nor did it think that arbitration would impinge upon the role of the Equal Employment Opportunity Commission. It also rejected the petitioner's procedural objections to arbitration, including his claims that arbitral panels would be biased, that discovery is limited in arbitration, that arbitrators did not have to issue written opinions, that class actions were unavailable in arbitration, and that arbitrators could not issue broad equitable relief. Finally, the Court had this to say about the claim of disparities in bargaining power: "Mere inequality in bargaining power, however, is not a sufficient reason to hold that arbitration agreements are never enforceable in the employment context."[28] Instead, such claims had to be evaluated on a case-by-case basis.

In two more cases, the Court underscored the point made in *Prima Paint* that arbitration clauses had to be considered separately from the rest of the contract: *Allied-Bruce Terminix Companies, Inc. v. Dobson*,[29] and *Doctor's Associates, Inc. v. Casarotto*[30]. Applying the principle of broad federal preemption it had announced in *Southland*, the Court held that states could not adopt specific statutes invalidating arbitration clauses; only the kind of flaw that would invalidate a general contract could be used to strike down such a clause. As the Court put it in *Allied-Bruce*, the basic purpose of the FAA was "to put arbitration provisions on the same footing as a contract's other terms."[31] In that case, its decision to apply the broadest possible interpretation of the Commerce Clause to a contract between a bug extermination company and a homeowner caused it to find the FAA applicable and preemptive of an Alabama statute making written, pre-dispute arbitration agreements invalid and unenforceable. *Doctor's Associates* did the same thing with a Montana statute that merely provided that arbitration clauses would be unenforceable unless they were typed in underlined capital letters on the first page of the contract.

At least one remaining question existed about the reach of the FAA until 2001: what did section 1 mean when it excluded from coverage "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce"? [32] Every court of appeals except the Ninth Circuit had held that this exempted contracts of employment for transportation workers, but not for any others. The Ninth Circuit thought

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28 *Id.* at 33.

29 513 U.S. 265, 281 (1995).

30 517 U.S. 681, 688 (1996).

31 *Id.* at 275 (internal quotations omitted).

32 9 U.S.C. § 1 (2000).

otherwise, and so the Supreme Court took the case of *Circuit City Stores, Inc. v. Adams*[33] to resolve the conflict.

In *Circuit City,* the Court reviewed once again the history of the FAA, reiterating that it "was a response to hostility of American courts to the enforcement of arbitration agreements, a judicial disposition inherited from then-longstanding English practice."[34] Using a variety of canons of statutory construction, the Court concluded that the Ninth Circuit's reading of the text of the statute was wrong. The exemption was the narrow one understood to exist in the other courts of appeals. It brushed aside the *amicus curiae* submission by the attorneys general of 22 states, who had argued that the inclusion of ordinary employment agreements under the FAA would intrude too deeply on the policies of the several states. As for that, the Court replied, their quarrel was with *Southland*'s preemption finding, and their remedy lay in Congress.

Only a few glimmers of caution have appeared in this otherwise impressive story of support for arbitration from the Supreme Court. One was in *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Junior University*.[35] In *Volt*, the parties had entered into a construction contract under which Volt was to install some electrical conduits on the campus of Stanford University. The contract had an arbitration clause, and it also had a choice-of-law clause that said simply that "[t]he Contract shall be governed by the law of the place where the Project is located."[36] That place was, of course, California. Problems arose; Volt filed a formal demand for arbitration; and Stanford responded with a state court action against Volt for fraud and breach of contract. Stanford's complaint also named two other defendants with whom it did not have arbitration agreements. Volt petitioned the state court for an order compelling arbitration, while Stanford asked the court to stay the Volt arbitration pending the resolution of the related litigation against the additional parties. The court did so, and the question whether that action was compatible with the FAA reached the U.S. Supreme Court.

Finding that the FAA, while preempting state laws, did not "occupy the entire field" of arbitration altogether, the Court held that the California law permitting the stay of arbitration was not preempted under the circumstances of this case. It placed considerable weight on the fact that the parties had agreed to use California law, and said that "[i]t does not follow that the FAA prevents the enforcement of agreements to arbitrate under different rules than those set forth in the Act itself."[37] It went on to hold that

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33 532 U.S. 105 (2001).

34 *Id.* at 111.

35 489 U.S. 468 (1989).

36 *Id.*

37 *Id*. at 479.

> [w]here, as here, the parties have agreed to abide by state rules of arbitration, enforcing those rules according to the terms of the agreement is fully consistent with the goals of the FAA, even if the result is that arbitration is stayed where the Act would otherwise permit it to go forward.[38]

Volt is not an anti-arbitration decision by any stretch of the imagination, but it offers a possible avenue back toward state laws that may be more protective of the arbitral process than might have seemed possible for a time. Another decision was also more nuanced. In *First Options of Chicago, Inc. v. Kaplan*,[39] the Court confirmed the fact that courts still have a role to play in both the referral of cases to arbitration and in the decision whether to confirm an arbitral award. Not uncommonly, a dispute will arise about the question whether a particular controversy is subject to arbitration at all: is there an arbitration agreement? does it cover these parties? does it cover this subject matter? The Court recognized that the question of who will decide "whether the parties agreed to arbitrate" is central. If the parties did not agree to submit that threshold question to arbitration, then (as had been true for many years in the area of labor arbitration) the court will decide independently. If they did agree that the arbitrator would resolve even arbitrability issues (and the court would have to decide at least this much), then that is what must happen. In making that determination, the court applies ordinary state-law contract law. It does so, however, without the usual strong presumption in favor of arbitration. The strong pro-arbitration presumption is reversed here: "[c]ourts should not assume that the parties agreed to arbitrate arbitrability unless there is clear and unmistakable evidence that they did so."[40] This is done because arbitration is a creature of agreement; without an agreement to arbitrate, it cannot exist. With respect to the second issue – standard of review for courts of appeals reviewing district court decisions about confirmation of awards – the Court held that ordinary standards should apply. There is no reason to give extra leeway to district courts that uphold arbitral awards.

This is hardly a comprehensive look at the Supreme Court's decisions in the area of arbitration. It is enough, however, to make the point that the Court has taken strong positions on the acceptability of arbitration as a co-equal method of dispute resolution, on the preemptive force of the FAA as an exercise of Congress's Commerce Clause power out to the furthest limits, on the typical inability of the states in the face of this federal legislation to enact arbitration-specific regimes that are less favorable to the process than the FAA would be, and on the lack of any subject-matter restrictions on arbitrable

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38 *Id.*

39 514 U.S. 938, 947 (1996).

40 *Id.*

claims. Against this background, we can turn to the issues courts are grappling with today. Some of these will look familiar, and some are newer, but all take on extra importance as arbitration itself becomes a firmly established part of the legal landscape.

II. CURRENT ISSUES

In the area of international trade regulation, which I have spent some time studying, the metaphor of a lake whose water level falls is common-place. It is used to describe the discovery of barriers to international trade that were hidden before formal tariffs or quantitative restrictions were abolished. As the tariff level – or water – falls, new problems become visible. With the lake, those newly visible things may be rocks or crevasses that no one realized were there before; with trade barriers, they might be private arrangements that impede international trade. I suggest that the same metaphor might help us understand what is happening today with arbitration. There is no doubt that the FAA, as it has been construed by the Supreme Court for more than three quarters of a century, has solved the problem of court hostility to arbitration and other alternative methods of dispute resolution. But, just as with our lake, the decrease in hostility to arbitration has revealed a new set of issues that must be addressed, lest we find ourselves simply trading one set of difficulties for another. Many of these newer problems are showing up in cases presently before the courts. What follows is my own list of some of the more significant ones I have observed.

A. *Arbitration Agreements*

The first set of issues, not surprisingly, concerns the arbitration agreement. Is there an agreement at all between these parties? If so, how much does it cover? Who are the parties, and despite the statements from the Supreme Court just reviewed, should it matter if they are unequal? Who will pay for the arbitration? Is one payment system inherently more fair than another? What law will govern the agreement and the arbitrators?

1. *Scope of the arbitration agreement*

Because the entire edifice of arbitration law is built upon agreement, it is appropriate for courts to compel arbitration only when the subject matter of the dispute falls within the scope of the agreement. The Supreme Court indicated as much in *First Options,* among many other cases. Section 2 of the FAA expressly refers to a "contract evidencing a transaction involving commerce to settle by arbitration a controversy," or other kinds of agreements in writing to submit disputes to arbitration.[41] This may seem like a mere formality, but it is not. Agreements to arbitrate disputes "arising out of" a

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[41] 9 U.S.C. § 2 (1994).

contract are narrower than agreements to arbitrate disputes "arising out of or related to" a contract. A dispute resolution clause that commits the parties to arbitrate any "invoice amount" does not obligate the parties to arbitrate claims about unlawful retention of documents.[42]

Another question that can arise is whether the parties in question have entered into an agreement at all. This was the issue in a recent Seventh Circuit case, *International Brotherhood of Electrical Workers, Local 176 v. Balmoral Racing Club, Inc.*[43] In that case, a company had terminated an agreement with one union, and then had begun working with another group of workers under the same terms and conditions.[44] One of those terms was an arbitration agreement.[45] The company argued that the agreement never extended to the new workers, while the union argued that it did.[46] Relying on the agreement's provisions for determining disputed issues of coverage, the court ruled that the workers were covered by the arbitration agreement.[47]

2. *Fee arrangements*

One of the most important current issues concerns the way in which the costs of arbitration will be allocated. For years, the Supreme Court and other courts have assumed that arbitration is an inexpensive, speedy alternative to traditional court dispute resolution. But that may be too simplistic. The first question is, compared to what kind of court? A court of general jurisdiction? A small claims court? The second is what kinds of costs should be anticipated. Discovery costs may be higher in the courts (although in this era of ever-increasing judicial management of the pre-trial process, that may be less true than it once was), but there is often *some* discovery in arbitration as well. If there is not, then a problem of a different character may exist, relating to the fairness of the overall procedure. I consider that in a few moments. Courts, as public institutions, are close to free: the price of admission is a small filing fee. Judges are not paid by the parties. Arbitrators, of course, work for pay. If the procedure is being handled by a single arbitrator, the fees may be more manageable, but if a panel of three arbitrators is used, fees can mount quickly. In some small claims cases, arbitration may not be any less expensive than the judicial process; it might be more.

The Supreme Court touched lightly on this subject in *Green Tree Financial Corp.-Alabama v. Randolph.*[48] In that case, the Court looked at the

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42 *See* Welborn Clinic v. Medquist, Inc., 301 F.3d 634, 640 (7th Cir. 2002).

43 293 F.3d 402 (7th Cir. 2002).

44 *Id.* at 403.

45 *Id.* at 404.

46 *Id.*

47 *Id.* at 407-08.

48 531 U.S. 79 (2000).

question "whether an arbitration agreement that does not mention arbitration costs and fees is unenforceable because it fails affirmatively to protect a party from potentially steep arbitration costs."[49] In keeping with its usual reluctance to make generalized anti-arbitration assumptions, the Court declined to make any systematic assumptions. But, it noted, "[i]t may well be that the existence of large arbitration costs could preclude a litigant such as Randolph from effectively vindicating her federal statutory rights in the arbitral forum."[50] Faced with a lack of information in the record about the actual costs the plaintiff would bear, the Court could not find the agreement unenforceable on that ground.[51] To hold otherwise, it remarked, would undermine the liberal federal policy in favor of arbitration and would be inconsistent with earlier rulings imposing the burden of proof on the party who argues that certain issues are unsuitable for arbitration.[52] Footnote 6 of the opinion explains the deficiencies in the plaintiff's proof; it strongly indicates that parties attacking arbitration on cost grounds had better be prepared with detailed information to back up their arguments.[53]

Courts have not been sure what to make of *Green Tree*'s rule. On the one hand, if parties are required to split costs evenly, the arbitration may be unduly burdensome to a consumer or employee party. Worse, a rigid rule of fifty-fifty cost-sharing might be inconsistent with statutes such as Title VII that give a right to 100% of attorneys' fees to a prevailing plaintiff.[54] Yet parties can waive many rights – even constitutional rights – if they do so with their eyes open, and so some courts have wondered why the right to receive attorneys' fees cannot also be waived in an arbitration agreement.[55] But, on the other hand, if the more powerful party pays 100% of the fees to the arbitrator or the arbitral body, is the process itself distorted? Can the arbitrator under those circumstances be unbiased, or is he or she more like the judge in the old case of *Tumey v. Ohio*,[56] who was paid from the fines he collected (and who the Supreme Court said was not the unbiased decisionmaker that the due process clause guarantees)? Perhaps the most that can be said with confidence is that when arbitration moves away from the classic areas of commercial transactions between roughly equal parties and collective

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49 *Id.* at 82.

50 *Id.* at 90.

51 *Id.* at 91.

52 *Id.*

53 *Id.* at 90 n.6.

54 *See, e.g.*, McCaskill v. SCI Mgmt. Corp., 298 F.3d 677 (7th Cir. 2001) (separate opinions discussing this point).

55 *See* Metro East Ctr. for Conditioning & Health v. Qwest Communications Int'l Inc., 294 F.3d 924 (7th Cir. 2002).

56 273 U.S. 510 (1927).

bargaining agreements, where the existence of the union assures much the same equality, new problems related to costs become apparent and are starting to demand resolution.

3. *Type of parties*

This takes us to the next question: who are the parties in modern arbitration settings? No one has dropped out of the picture, to be sure. Arbitration still plays a key role in the law of industrial relations. Its importance has always been great in international business transactions, and there is no reason to anticipate a change in that fact. Organized markets have used arbitration since the time of Medieval England, and they continue to do so today. What is different, at least in the American experience, is the extent to which arbitration is being imposed on consumers, credit card holders, employees, and other individual parties who generally lack any ability to negotiate or to resist any term of the trade. The American Arbitration Association recognizes the differing dynamics between commercial and consumer arbitration, and it has developed separate rules for each type. That distinction has not yet made a formal appearance in judicial decisions, however, and the Supreme Court's *Green Tree* decision and its rulings in analogous cases like *Carnival Cruise Lines, Inc. v. Shute*,[57] which upheld a choice-of-forum clause in a consumer transaction even though the clause appeared in tiny print and was buried in the back of a cruise ticket, indicate that the Court is not ready to take that step yet.

4. *Governing law*

Although it may seem too late in the day to question whether the FAA has full preemptive force over state laws that attempt to protect consumers, franchisees, employees, or others with a perceived lack of bargaining power from having arbitration imposed upon them, given the Supreme Court's repeated reaffirmations of *Southland*, one should not make hasty assumptions. Some might have thought that the jurisprudence of the Eleventh Amendment was well settled before the Court decided *Seminole Tribe* in 1996,[58] but they would have been wrong. *Lopez*[59] was another unexpected constriction on Congress's Commerce Clause power, and a few years later, *Morrison*[60] underscored the fact that detailed congressional findings about the effect of the prohibited practice on interstate commerce were not going to dissuade the Court from making an independent determination. While no one (to my knowledge) expects that the Court will conclude that some transactions –

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57 499 U.S. 585 (1991).

58 517 U.S. 44 (1996).

59 United States v. Lopez, 514 U.S. 549 (1995).

60 United States v. Morrison, 529 U.S. 598 (2000).

perhaps like the home termite inspection contract in *Allied-Bruce*[61] – have such a minimal effect on interstate commerce that Congress *cannot* reach them, other forms of retrenchment are possible. For example, in *Jones v. United States*,[62] the Court concluded that the federal statute criminalizing arson of a building that affected interstate commerce had to be construed narrowly, lest constitutional questions arise.[63] There is nothing to prevent the Court from re-visiting its expansive interpretation of section 2 of the FAA (which several members of the Court have continued to criticize, even as they respect the rule of *stare decisis*) and deciding that the FAA does not have the broad substantive preemptive force it is now given.

B. *Arbitral Process*

A second broad set of issues that is moving to the fore has to do with the procedures that govern the actual arbitration proceeding. Traditionally, this is a subject that has been left to the parties. Some arbitration agreements call for the use of an off-the-shelf set of procedures, such as the rules of the American Arbitration Association, or the International Chamber of Commerce, or the United National Conference on International Trade Law (known commonly as UNCITRAL); others say nothing at all on the subject, and allow the arbitrator to make up the rules as he or she goes along; while others are using the facilities of industry-specific organizations, such as the National Association of Securities Dealers.[64] However the rules are chosen, they are coming under increasing scrutiny.

1. *Who are the arbitrators?*

The first question relates to the identity and qualifications of the arbitrators. If the parties have agreed to submit their dispute to a single arbitrator, then there is a premium on assuring that this person will be an unbiased decisionmaker. If they have agreed to use three arbitrators, then commonly each party will be entitled to designate a party-arbitrator, and then some system will be used to select the neutral tie-breaker. Courts have found no fault with the presence of the party-arbitrators on the panel[65]; that system

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61 Allied-Bruce Terminix Co. v. Dobson, 513 U.S. 265 (1995).

62 529 U.S. 848 (2000).

63 *Id.* at 858.

64 *See, e.g.*, Miller v. Flume, 139 F.3d 1130 (7th Cir. 1998) (investor claims were arbitrable under the NASD Code of Arbitration Procedure).

65 *See, e.g.*, Sphere Drake Ins. Ltd. v. All American Life Ins. Co., 307 F.3d 617 (7th Cir. 2002). This opinion goes even further than the statement in the text. It states that "[t]o the extent that an agreement entitles parties to select interested (even beholden) arbitrators, section 10(a)(2) [of the FAA, reproduced below] has no role to play." *Id.* at 620. Not all judges would subscribe to the last comment, at least if it were extended to a single party's imposition of an

(*continued*)

simply focuses attention on the third arbitrator. For present purposes, there is no need to distinguish between the single arbitrator and the third neutral.

Established arbitral institutions like the AAA maintain lists of qualified arbitrators, have rules for the disclosure of conflicts of interest, and otherwise have measures in place to assure that the arbitrator can command the trust and respect of both parties. The risks in this area come more from the *ad hoc* procedures or from institutions operated by representatives of only one side of potential disputes: industry associations, employer associations, or even lists of arbitrators created only by the party with greater resources. Courts have not wanted to assume partiality in these arrangements, but it is easy to detect an unease that has prompted some courts to refuse to enforce awards in the more egregious situations.[66]

2. *Development of the facts*

One of the most important differences between arbitral procedures and court procedures is the absence of traditional American-style discovery in the former. This is surely a major contributor to the cost savings that are thought to accompany arbitration (although it would be helpful if someone would undertake a rigorous study of the cost differences between the two systems, adjusting for type of case, to see if there is any empirical basis for the assumption). But there is a dark underside to this too. Without the powers of the court behind the weaker party, it can be very difficult to gather information in the opponent's possession that may throw important light on the case. Even in a straightforward employment dispute, where the plaintiff believes that she was not promoted because of her age, or her gender, or her religion, it is often necessary to find out how the employer has treated others similarly situated to the plaintiff. No litigant wants to turn over unfavorable information to an opponent, but the courts can take steps to ensure that required discovery takes place. Arbitrators do not have the same power to do so, and the arbitral rules used often place strict limits on document discovery, the number of depositions that will be permitted, and the matters that may be explored.

3. *Confidentiality*

The courts, as everyone knows, are public institutions. One of the prices of submitting a dispute for resolution in a court is the loss of privacy that would otherwise exist. If there is a legitimate reason to restrict distribution of certain materials, it is of course possible to obtain a protective order from the court, but protective orders are not granted promiscuously. Broad stipulations that materials will be maintained under seal are not good enough for the

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interested arbitrator upon another party who had no ability to prevent such a choice.

[66] Some of those cases are discussed below.

appellate courts, which insist that the parties explain, document by document and paragraph by paragraph, if necessary, why the presumption of open courts should be disregarded in their case.

Arbitration is completely different. Everything, from the content of the demand for arbitration, through the materials submitted before the hearing, the hearing, and the ultimate reasons for the disposition, can be, and often is, maintained in absolute confidence. Indeed, this is an important reason why arbitration is attractive to many parties. Employers might like to keep a veil over information like how many discrimination complaints are filed against them; doctors might like information about malpractice allegations to be hard or impossible to find; manufacturers might like to prevent information about product liability settlements from seeing the light of day; and franchisors might like to keep the details of their disputes with franchisees secret. If so, then arbitration holds great attraction for them. Employees, patients, customers, and franchisees may see fewer benefits in the confidentiality provisions – and it is a fair bet that the plaintiffs' bar is no fan of arbitral secrecy.

4. *Written explanations of results*

While courts have expressed comparatively little concern with arbitral confidentiality, the absence of any requirement in the FAA or elsewhere in the law for arbitrators to offer an explanation of their decision has become a source of increasing attention. This may not have been a problem, and it may not even now be a problem, when private parties are resolving private contractual disputes. In such cases, the law is relatively indifferent to the ultimate truth of the matter – who was right, who was wrong, who breached, who shipped a defective product – and instead it emphasizes the social harmony that comes from successful dispute resolution. Statutory claims are different. No one would argue that society as a whole is uninterested in the accurate and fair application of the laws forbidding discrimination on invidious grounds, or the laws regulating securities markets and transactions, or the antitrust laws, or the laws governing consumer credit transactions. Yet how can anyone be sure that those laws were competently and accurately applied in an arbitration proceeding, if no one knows whether one arbitrator flipped a coin to reach his result, or if another arbitrator conducted a painstaking study of the relevant rules and reached a reasoned conclusion. And even in the case of the second arbitrator, what if that reasoned conclusion turns out to be wrong? District court judges are required to do no less, and they are reversed from time to time by appellate courts (something like 15% of the time, if the statistics from the Administrative Office of the U.S. Courts paint a representative picture). The combination of confidentiality and the lack of a requirement for an explanation (written or recorded on an accurate transcript) create a troubling possibility of important public laws that may be unenforced, or mistakenly enforced.

5. *Costs (again)*

Even if the parties have not specified in their arbitration agreement how to allocate costs, along the lines discussed above, costs can arise as a problem within the arbitration proceeding itself. Someone will have to decide who pays the arbitrator's fees, who pays the other fixed costs of conducting the proceedings (such as rent for the space used, storage for documents, and the like), and how attorneys' fees will be allocated. For the reasons already mentioned, the way in which these costs are distributed can affect the overall accessibility of the arbitral procedure to aggrieved parties.

C. *Recognition and Enforcement of Awards*

No case could have emphasized more strongly that the presumption in favor of arbitration operates at its strongest at the beginning of the process, when a court is faced with the question whether to compel arbitration (or to enforce an agreement to arbitrate), than did *Mitsubishi v. Soler Chrysler-Plymouth*.[67] In that decision, the Supreme Court found reason in the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards to compel arbitration of an international antitrust dispute, relying on Article II, paragraph 1, of the Convention.[68] The Court recognized that a panel of Japanese arbitrators applying Swiss law (the law chosen in the contract at issue) might not give full force to U.S. antitrust laws, but it said that any such problem could be addressed at the end of the process, when the winning party sought recognition and enforcement of the eventual award. It seems, however, that the Court may have been unduly optimistic about the practical availability of post-arbitral review, either under the New York Convention or under the FAA itself. For a number of good reasons, most having to do with the preservation of arbitration as a true alternative to the courts, and not just a preliminary step along a long road, courts have read the FAA as imposing very strict restrictions on the grounds that would justify overturning an arbitral award.[69] With few exceptions, therefore, once a case has been entrusted to arbitration, no court will ever do anything with it again.

1. *FAA standard of review*

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[67] Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc., 473 U.S. 614 (1985).

[68] *See id.* at 639. The New York Convention was implemented in the United States, in Chapter 2 of Title 9 of the U.S. Code. See 9 U.S.C. §§201 et.seq.

[69] *See, e.g.*, Flexible Mfg. Systems Pty. Ltd. v. Super Products Corp., 86 F.3d 96 (7th Cir. 1996) ("If courts were to undertake the kind of searching review of arbitral awards that Super Products invites here, arbitration would be transformed from a commercially useful alternative method of dispute resolution into a burdensome additional step on the march through the court system.").

Perhaps the best illustration of the point just made comes from the text of the FAA itself. Section 10(a) sets forth the grounds on which a court is permitted to set aside or vacate an arbitral award. It reads as follows:

> In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration –
>
> (1) where the award was procured by corruption, fraud, or undue means;
>
> (2) where there was evident partiality or corruption in the arbitrators, or either of them;
>
> (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or
>
> (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.[70]

This is hardly a long list. Conspicuously absent from it are grounds such as mistake of fact (even under a deferential standard of review like the "clearly erroneous" rule of Federal Rule of Civil Procedure 52),[71] mistake of law, abuse of discretion, or any other familiar theory that might prompt a party to take an appeal from an adverse result in a trial court. The first ground – corruption, fraud, or "undue means" – is fairly self-explanatory and (thankfully) does not arise often. The second, as noted above, has been construed narrowly by courts. "Evident" partiality means something far worse than an appearance of impropriety.[72] Similarly, while section 10(a)(3) might seem to invite serious review of the actual conduct of the arbitral proceeding, ranging from rulings on motions for extensions of time, to discovery disputes,

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[70] 9 U.S.C. § 10(a) (2000).

[71] Fed. R. Civ. P. 52.

[72] As the decision in Sphere Drake Insurance Ltd. v. All American Life Insurance Co., 307 F.3d 617 (7th Cir. 2002), pointed out, there is some value still in comparing the standards for disqualifying judges with the standards to be used in assessing arbitrator impartiality. If a judge similarly situated to the challenged arbitrator would *not* have to recuse herself, then it is clear that the arbitrator did not have the kind of "evident partiality" that would require disqualification. *Id* .at 622. It is the converse that is not true: under 28 U.S.C. § 455 (2000), there will be instances in which a judge would have to recuse herself, but that do not rise to the level of "evident partiality."

to handling of witnesses, that is not how the courts have construed it. Mistakes are not the same thing as "misconduct," and only the latter would permit judicial intervention. The last ground, in contrast, has some bite. If the arbitrators went beyond the scope of the arbitral agreement, then they exceeded their powers. Courts will refuse to enforce arbitral awards that cannot be traced to the parties' agreement to arbitrate. They may also refuse to enforce an award that is so vague, or inconclusive, or interlocutory, that no one can tell what it requires.

2. *Review for mistakes of fact*

As already noted, straightforward review for mistakes of fact simply does not happen. Parties on both sides should realize that when they bargain for arbitration, they are bargaining for the decision of one and only one body on the facts of their case. Objectively speaking, this is not a factor that necessarily will favor one side or the other. In an employment case, for example, if the arbitrator chooses to believe the complaining party's version of the events, the employer might wish it had another chance. This aspect of arbitration has been widely accepted, even though the arbitrator's findings of fact will be influenced by the evidence the parties are able to collect, and thus might reflect an unconscious bias toward the side with better access to the information.

3. *Review for mistakes of law: "manifest disregard"*

Courts also refuse to review arbitral awards for mistakes of law – or at least, for ordinary mistakes of law. Review of legal conclusions is not among the grounds listed in FAA section 10(a), and one might think that this is the end of matters. It is not. As far back as *Wilko v. Swan*, the Supreme Court suggested that an arbitrator's "manifest disregard" of legal rules might justify judicial intervention.[73] But this has proven to be a difficult standard to apply, because it requires courts to draw the line between the kinds of mistakes of law that fall outside the boundaries of judicial review, and those that are either different in kind or so different in degree that they represent "manifest" disregard.

The Second Circuit confronted this problem squarely in *Greenberg v. Bear, Stearns & Co.*,[74] where it offered the following reconciliation between section 10 and this additional ground of judicial review:

> The FAA and federal case law supply various bases for review of an arbitral award. Section 10 itself lists several grounds, including fraud in procuring the award; corruption, partiality, or prejudicial misconduct on the part of the

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[73] 346 U.S. 427, 436-37 (1953).

[74] 220 F.3d 22 (2d Cir. 2000).

> arbitrators; abuse of power; and failure to render 'a mutual, final, and definite award.' 9 U.S.C. § 10(a). Judicial interpretation has added additional grounds, such that awards may be vacated under limited circumstances where the arbitrators manifestly disregarded the law . . . or where enforcement would violate a "well defined and dominant public policy.[75]

It went on to say that manifest disregard existed only if the reviewing court found "both that (1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether, and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case."[76]

The Seventh Circuit has taken a far more circumscribed approach to the "manifest disregard" standard. In *George Watts & Son, Inc. v. Tiffany & Co.*,[77] the court, relying to a significant degree on the Supreme Court's decision in *Eastern Associated Coal Corp. v. United Mine Workers*,[78] offered the following alternative interpretation to the idea of "manifest disregard" review:

> . . . [A]n arbitrator may not direct the parties to violate the law. In the main, an arbitrator acts as the parties' agent and as their delegate may do anything the parties may do directly.[79]

Under this standard, the arbitrator who knows about the law and deliberately refuses to follow it is insulated unless the legal norm in question is an unwaivable, mandatory rule of law and the failure to enforce it amounts to an order to do something illegal. As the concurring judge in *George Watts* noted, this is a major step to take.[80] The conflict in the circuits that this may have created continues to exist. All that can be said at present is that there is a felt need in many quarters for some avenue of judicial review for the worst instances of misapplication of public regulatory laws, but that will be more readily available in some parts of the country than in others.

4. *Public policy review*

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75 *Id.* at 26-27 (internal citations omitted).

76 *Id.* at 28.

77 248 F.3d 577 (7th Cir. 2001).

78 531 U.S. 57 (2000) ("we must treat the arbitrator's award as if it represented an agreement between the parties themselves").

79 248 F.3d at 580.

80 *George Watts*, 248 F.3d at 581 (Williams, J. concurring).

Although, as the Second Circuit pointed out in *Greenberg*, U.S. courts have added "public policy" to the list found in section 10, in this instance foreign arbitral awards stand on a somewhat different footing.[81] The New York Convention, like the FAA, spells out the reason why recognition and enforcement of an award falling under the Convention may be rejected, and the list is not quite the same as the one in the FAA. Article V of the Convention reads as follows:

> 1. Recognition and enforcement of the award may be refused, as the request of the party against whom it is invoked only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:
>
> (a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or
>
> (b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or
>
> (c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or
>
> (d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or
>
> (e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.

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[81] Greenberg v. Bear, Sterns & Co., 220 F.3d 22 (2d Cir. 2000).

> 2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:
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> (a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or
>
> (b) The recognition and enforcement of the award would be contrary to the public policy of that country.[82]

Aside from the point that is immediately relevant here, which is that the Convention expressly recognizes in Article V.2(b) that public policy is a valid reason for refusing to enforce an arbitral award, while FAA section 10 does not, it is worth comparing the result of the reasons set forth in Article V to their counterpart in section 10 as well. The Convention appears to give more flexibility to reviewing courts to assess which subject matters are capable of resolution by arbitration, whether the parties received adequate notice of proceedings, whether there were disqualifying flaws in the arbitral procedure, and a number of other points that have arisen in domestic cases. To the extent that the spread of arbitration prompts study of the domestic regime in the United States, it may be fruitful to look at experience around the world with the New York Convention to see if some cross-fertilization from the international system would be desirable. Internationally, it would have been unthinkable not to provide for a "public policy" safety valve, when courts are asked to enforce an award made in a different country, under different rules. Whether such a rule exists for domestic proceedings (particularly given the scope of federal preemption that presently exists, which leaves no room for states to have different public policies) is just as debatable as the "manifest disregard" rule.

5. *Fundamental fairness review*

Fundamental fairness might refer to substantive outcomes, or it might refer to the procedures used. If it is the former, then we run back into the problem of the essential unreviewability of facts and law, except to the extent that there is a "manifest disregard" exception. If it is the latter, then it is necessary to look at section 10 again to see what kinds of procedural protections it affords. The answer is that it provides some protection: parties are guaranteed an arbitrator who does not display "evident partiality," they are assured a procedure that is free from fraud and corruption, and they may obtain relief from awards in excess of the arbitrator's powers. On the procedural side, the best way to make sense of a "fundamental fairness" ground for review would be to consult the basic due process decisions of the

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[82] Convention on the Recognition and Enforcement of Foreign Arbitration Awards, June 7, 1959, art. 5, 21 U.S.T. 2517, 330 U.N.T.S. 38; 9 U.S.C. §201 note.

Supreme Court, look for the bare minimum, and see whether that level is assured. Notice, an unbiased decisionmaker, and an opportunity to be heard are generally considered the bedrock principles of due process, and these may not be beyond the reach of a reviewing court, if the party attacking the award can demonstrate that they were absent.

6. *Agreements to expand FAA review*

Last in our list of newer developments is the possibility that the parties might be able to contract for more comprehensive judicial review than the FAA or other sources of positive law like the New York Convention give them. The idea is simple: if arbitration is really a creature of agreement, then why can parties not agree to judicial review of their arbitral award – plenary review, limited review, or something in between. Like many superficially simple ideas, however, this one sits on top of a more complex reality. At present, there is a conflict in the circuits over the permissibility of this maneuver. The Seventh, Eighth and the Tenth Circuits take the position that private parties cannot modify the public process of judicial review through private agreements.[83] In contrast, the Fifth[84] and Ninth[85] Circuits have seen enhanced judicial review as consistent with the broader preference for private ordering (cafeteria-style public judicial services?) and honoring party agreements. The desire to be able to modify the FAA is understandable enough. Most of the criticisms one hears have to do with the fact the important public policies are being developed without any way of ensuring consistency and faithfulness to the purpose and intent of the statutes. If there were a way to move back into the court system at the endpoint, that problem would be solved. But it is a big step to assume that parties can pick and choose the procedural rules of the court that will apply to them. The question of what kinds of orders are appealable, and at what point in a proceeding, is one of the most important procedural rules courts have. Whether private agreements can opt back into the court system at the appellate level under the law as it now stands, and if not, whether it is even desirable to make that change in the law, is an issue intimately tied up with the scope of section 10 in the first place. My own view is that it would be preferable to work directly on amendments to section 10, if any change is to occur, than to create or expand a doctrine of optional appellate review.

III. RUMBLINGS IN THE COURTS

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83 *See* Bowen v. Amoco Pipeline Co., 254 F.3d 925 (10th Cir. 2001); UHC Mgmt. Co. v. Computer Sciences, 148 F.3d 992 (8th Cir. 1998); and Chi. Typographical Union v. Chi. Sun-Times, 935 F.2d 1501 (7th Cir. 1991).

84 Gateway. Techs., Inc. v. MCI Telecomm. Corp., 64 F.3d 993 (5th Cir. 1995).

85 Lapine Tech. Corp. v. Kyocera Corp., 130 F.3d 844 (9th Cir. 1997).

It would be wrong to overstate the current significance of the concerns about arbitration that have just been reviewed. The courts still regularly enforce agreements to arbitrate; they stay proceedings or dismiss them outright so that arbitration can take place; and they enforce arbitral awards even when they are told convincingly that the arbitrator made mistakes of fact or law. At the same time, as the review of Supreme Court cases illustrates, the field within which arbitration operates has expanded to cover virtually everything except the criminal law. But lately, in a surprising number of appellate courts, one finds decisions refusing to go along with arbitration systems that seem too unfair, declining to recognize agreements to arbitrate in arrangements that appear to the court to be unconscionable, finding a lack of consideration to support particular agreements to arbitrate, and for other reasons declining to take arbitration out to its logical limits. These decisions may be nothing more than the exceptions that prove the rule, or they may be the harbingers of a more serious re-thinking of the law of arbitration. It is worth knowing that they are out there, however, because in the aggregate they suggest that arbitration (like free markets) cannot be utterly unregulated. What follows is a brief overview of the cases that have balked at supporting arbitration in one way or the other.

A. *Fees*

Once again, because of the prevalence of the fee issue, I begin there. Five decisions have found problems in one way or the other with one-sided fee arrangements. The earliest was *Cole v. Burns International Securities Services.*[86] In that case, the D.C. Circuit held that an employer may not condition employment on the employee's acceptance of an arbitration agreement that requires the employee to submit his or her statutory claims to arbitration and to pay all or part of the arbitrator's fees.[87] The Tenth Circuit ruled similarly in *Shankle v. B-G Maintenance. Management. of Colorado, Inc.*,[88] when it held that a mandatory arbitration agreement that was entered into as a condition of continued employment, and which required the employee to pay just a portion of the arbitrator's fees, was unenforceable under the FAA.[89] Another case in which the imposition of the responsibility to pay fees on the employee was potentially fatal to the enforcement of the arbitral agreement was the Fourth Circuit's decision in *Bradford v. Rockwell Semiconductor Systems, Inc.*[90] That court held that a fee splitting provision in an employment agreement that required the employee to share the costs of

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86 105 F.3d 1465 (D.C. Cir. 1997).

87 *Id.* at 1483-84.

88 163 F.3d 1230 (10th Cir. 1999).

89 *Id.* at 1233-34.

90 238 F.3d 549 (4th Cir. 2001).

arbitration could, but did not necessarily, render a mandatory arbitration agreement unenforceable if the arbitration fees and costs would be so high that they would effectively deny the employee access to the arbitral forum.[91] That, of course, is what the Supreme Court also said in *Green Tree*. The Seventh Circuit's decision in *McCaskill v. SCI Management. Corp.*,[92] while the product of a deeply split panel, concluded that a provision in an arbitration agreement requiring each party to pay its own costs and attorneys' fees was unenforceable, in the face of the statutory right of prevailing plaintiffs in Title VII cases to obtain their fees.[93] Another panel of the Seventh Circuit then questioned this result,[94] but the point here is less about where the law of the Seventh Circuit may be at the moment and more about the prevalence of expressed concerns on the fee question. Finally, when the Ninth Circuit received the *Circuit City* case on remand from the Supreme Court, it refused to enforce the arbitration agreement on a number of grounds.[95] One of the grounds that contributed to the court's conclusion that the arbitration agreement was substantively unconscionable was the fact that it required the employee to split the arbitrator's fees with the employer.[96]

B. *Employer-biased process*

The fee-splitting requirement was not the only problem with the *Circuit City* agreement, as the Ninth Circuit saw it. Overall, it thought that the process was unacceptably biased in favor of the employer.[97] It unilaterally forced employees to arbitrate all employment-related claims against the employer, but it placed no such restriction on the employer's choice of forum; it limited the relief available only to employees; it had the fee-splitting rule just noted; and it imposed a strict one-year statute of limitations on arbitrating claims, which was narrower than the time period they would have had for continuing violations under California law.[98] The agreement the Fourth Circuit refused to enforce in *Hooters of America, Inc. v. Phillips*[99] was also transparently biased in favor of the employer. The Hooters arbitration rules required, among other things, that all arbitrators be selected from a list created by the employer, that there would be no limits on who Hooters could place on the list, that

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91 *Id*. at 554.

92 298 F.3d 677 (7th Cir. 2002).

93 *Id*. at 680-86.

94 See Metro East Ctr. for Conditioning & Health v. Qwest Communications Int'l, Inc., 294 F.3d 924 (7th Cir. 2002).

95 Circuit City Stores, Inc. v. Adams, 279 F.3d 889 (9th Cir. 2002).

96 *Id*. at 894.

97 *Id*.

98 *Id*.

99 173 F.3d 933 (4th Cir. 1999).

employees had to give notice of claims but that Hooters did not have to give notice of its defenses, and that only Hooters could expand the scope of the proceedings.[100] The Fourth Circuit found these rules so egregiously unfair that they represented a complete default of the employer's contractual obligation to draft the rules in good faith.[101] Another case in which a court found unacceptably biased rules was *Ticknor v. Choice Hotels International, Inc.*[102] Under Montana law, the court found, the arbitration clause before it was unconscionable.[103] The clause was contained in a standardized, form franchise agreement between a hotel chain and an operator.[104] Under this agreement, the chain could bring any claims against the operator in state or federal court, but the operator was forced to submit all claims to binding arbitration at the chain's Maryland headquarters.

C. *General unconscionability/unfairness*

Many of the cases focusing on the one-sidedness of an agreement also use the rhetoric of unconscionability: *Circuit City* on remand and *Ticknor* are two examples of this.[105] Several district courts have also refused to enforce arbitration agreements on general unconscionability grounds. In *Lozada v. Dale Baker Oldsmobile, Inc.*,[106] the district court found that an arbitration clause in a retail installment sales and security agreement relating to automobile sales was substantively unreasonable and unconscionable under Michigan law.[107] The clause provided for the waiver by buyers of the right to proceed by way of a class action. The court thought that this provision denied buyers the opportunity to sue as a group that those the federal Truth-in-Lending Act guarantees, as well as compromising their rights under state consumer protection law.[108] Linguistic difficulties prompted a district court in Texas to refuse to enforce an arbitration agreement.[109] In *Prevot v. Phillips Petroleum Co.*, employees who did not understand English had been pressured to sign arbitration agreements.[110] The agreements were not translated for them, and the court found that they did not know what they

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100 *Id*. at 938.

101 *Id*.

102 265 F.3d 931 (9th Cir. 2001).

103 *Id*. at 939-40.

104 *Id*. at 935.

105 *See* Circuit City Stores, Inc. v. Adams, 279 F.3d 889 (9th Cir. 2002) and *Ticknor*, 265 F.3d at 931.

106 91 F. Supp. 2d 1087 (W.D. Mich. 2000).

107 *Id*. at 1105.

108 *Id*. at 1104-05.

109 *See* Prevot v. Phillips Petroleum Co., 133 F.Supp.2d 937 (S.D. Tex. 2001).

110 *Id*. at 940.

were signing.[111] Under the circumstances, the court found the agreements to be procedurally unconscionable under Texas law.[112] Another district court wrote more broadly in *Rollins, Inc. v. Foster*.[113] Again along *Green Tree* lines, that court found that when a party who is in an inferior bargaining position is compelled to assert her claims in arbitration, and is thereby precluded from turning to less expensive public fora, and the costs of the arbitral forum render her unable to pursue her claim, the clause is oppressive and one-sided, and thus unconscionable.[114]

D. *Lack of consideration*

Recognizing the Supreme Court's emphasis on the need to invalidate arbitration agreements only for reasons that would apply generally to contracts, a number of courts have examined the consideration supporting the arbitration agreement before them and have found it to be wanting. Several decisions involving the restaurant chain Ryan's Steak House have rejected its arbitration system on this ground, including *Penn v. Ryan's Family Steakhouses Inc.*[115] and *Floss v. Ryan's Family Steakhouses Inc.*[116] In *Penn*, the court found that a contract between the employee and the arbitration service (not the employer, Ryan's), which the employee signed as a condition of his employment, was not enforceable under Indiana law.[117] The agreement provided that the employee had to use the service to arbitrate any employment-related disputes with Ryan's, and the service promised only to provide an arbitration forum, rules, procedures, a hearing, and a decision.[118] These were at best illusory and unenforceable promises on the part of the service, as there was nothing to limit its ability to amend the rules.[119] Furthermore, the court concluded that Indiana would not treat any promise made by the employer to Penn as substitute consideration. *Floss* found similar problems with the arrangement; it too was concerned about the service's unfettered discretion to change the rules and procedures at any time without any notice or consent from the employees.[120] *Gibson v. Neighborhood Health Clinics, Inc.*[121] presented a problem of prior consideration. There, the court

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111 *Id.*

112 *Id.* at 940-41.

113 991 F. Supp. 1426 (M.D. Ala. 1998).

114 *Id.* at 1437.

115 269 F.3d 753 (7th Cir. 2001).

116 211 F.3d 306 (6th Cir. 2000).

117 *Id.* at 761.

118 *Id.* at 755-56.

119 *Id.* at 757.

120 *See Floss*, 211 F.3d at 315-16.

121 121 F.3d 1126 (7th Cir. 1997).

found that under Indiana law an employee's promise to submit discrimination claims to arbitration was not supported by consideration in the form of the employer's promise to hire her or to continue to employ her, where she was already hired at the time she made the promise, and the employer never made any commitment that she could continue to work there.[122] The much earlier decision in *Hull v. Norcom, Inc.*[123] also insisted on real mutuality of promises. There, the Court said that the mere presence of an arbitration clause is insufficient to enforce the arbitration agreement; the consideration exchanged for one party's promise to arbitrate must be the other party's promise to arbitrate at least some specified class of claims.[124] *Dumais v. American Golf Corp.* was another case in which the employee signed an agreement to arbitrate after he was already hired.[125] In addition, this was another agreement in which the employee was bound, but the employer was free unilaterally to modify the terms of the arbitration agreement at any time.[126]

E. *Flaws related to notice*

The last set of cases involve concerns about the quality of the notice the employee received. In addition to the language problem noted in *Prevot*, there have been other cases in which arbitration clauses have not been enforced because of faulty notice. In *Kummetz v. Tech Mold, Inc.*,[127] the Ninth Circuit held that an employee did not, by signing an acknowledgment in an employee handbook, knowingly agree to arbitrate his employment discrimination claims under the Americans with Disabilities Act and the Arizona Civil Rights Act.[128] The acknowledgment did not mention or imply that the handbook contained an arbitration provision.[129] (Furthermore, in many handbook cases, employees attempt to persuade courts that they have a contractual right to continued employment, while employers point to handbook language announcing that the handbook does not create any enforceable legal rights. There is little chance that a court would permit an employer to have things both ways: either the handbook does create a contract, including a contract to submit claims to arbitration, or it does not.) In *Renteria v. Prudential Insurance Co. of Amercia*,[130] the court refused to find a knowing waiver of the right to litigate Title VII claims where neither the arbitration clause nor any

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122 *Id.* at 1131.

123 750 F.2d 1547 (11th Cir. 1985).

124 *Id.* at 1550.

125 150 F.Supp. 2d 1182 (D.N.M. 2001).

126 *Id.* at 1193.

127 152 F.3d 1153 (9th Cir. 1998).

128 *Id.* at 1155.

129 *Id.*

130 113 F.3d 1104 (9th Cir. 1997).

other written employment agreement expressly put the employees on notice that they were bound to arbitrate Title VII claims. Finally, in *Alphagraphics Franchising, Inc. v. Whaler Graphics, Inc.*,[131] the district court concluded that a forum selection clause applicable to an arbitration provision in a franchise agreement was not enforceable because of fraud in the inducement.[132] The franchisors had provided notice to franchisees in their offering circular that franchise agreements requiring arbitration to take place outside of Michigan were unenforceable under Michigan law, but they had conveniently failed to disclose that they planned to rely on the FAA in order to enforce the clause despite the state law.[133]

V. CONCLUSION

No one should question the utility of arbitration as a method of dispute resolution in a wide variety of contexts. In the international arena, it provides a vital and trusted way that business partners from different countries can arrange for the resolution of disputes that may arise in their commercial or other business transactions. It can do the same thing in purely domestic commercial relationships, where it is sometimes of great value to be able to choose a decisionmaker who is expert in the field, to take advantage of more flexible procedures, and to try to resolve disputes quickly and more or less harmoniously, so that the business can continue. Arbitration has served exactly that function for decades in the area of employer-union relations, where the promise of speedy industrial arbitration has served as a beneficial alternative to cruder tools like strikes and lock-outs.

The problems we are encountering today have come as arbitration has expanded to two new areas: consumer transactions, and statutory claims. The issues that each of these new areas raise are distinct, but they point in the same direction. If arbitration is to play a significant role in the enforcement of public law, then arbitration itself must become more publicly accountable. Accountability may not require any modifications in the general standards used to enforce agreements to arbitrate at the front end, but it may require a careful expansion of the grounds on which ultimate awards can be reviewed in the courts. With respect to consumer transactions, the formation of the agreement to arbitrate and the costs of the arbitral procedure are both matters of concern. Contracts of adhesion do not look much like the model of agreement that traditionally underlay arbitration. Perhaps a system requiring affirmative opt-in procedures, rather than the negative option most consumers typically receive now (i.e. if you continue to use your telephone, you have agreed to arbitrate), might be better. On the costs front, some consumer

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131 840 F. Supp. 708 (D. AZ. 1993).

132 *Id.* at 711.

133 *Id.*

arbitration agreements permit the consumer to use the local small claims court if the claim falls within that court's jurisdiction. That is an interesting idea, and one that deserves further study. Otherwise, the rules relating to costs must steer between the Scylla of employer/franchisor/company bias (where the more powerful party pays for everything and has a long-term relationship with the arbitration provider) and the Charybdis of pricing the less powerful party out of any dispute resolution forum at all (where costs are shared evenly). The use of established organizations like the AAA is one way to ensure neutrality, especially when the rules of procedure are tailored to the kind of case that is submitted.

Arbitration has a promising future, but if it is to serve all the functions that are now being demanded of it, it will need to adapt. Just as the courts themselves adapted over time, and developed special rules for family relations, special rules for small claims, and special rules distinguishing between civil and criminal proceedings, the process of arbitration will have to adapt as well. As that process unfolds, either the Congress or the Supreme Court may wish to consider whether it would be better to return to the fifty laboratories of legal development that the states can be, or if it is preferable to keep every kind of arbitration federalized for all purposes. Either way, experimentation will have to be the word of the day. Arbitration is here with us to stay, and it has now become our duty to make it as fair, as cost-effective, as true to the law, and as accountable as possible.